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REPORT ON EXCLUSIVE FOOD AND
BEVERAGE CONTRACT

CALIFORNIA STATE EXPOSITION AND FAIR

MAY 1973

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May 31, 1973

Honorable Pauline Davis, Chairwoman
Joint Committee on Fairs Allocation
and Classification
Room 4148, State Capitol
Sacramento, California 95814

Dear Pauline:

Transmitted herewith is the report on the Ancorp National Service, Inc., exclusive food and beverage contract with Cal Expo.

The operations of the contractor under the arrangement provisions of the federal Bankruptcy Act create the following problems.

- In the event the contractor becomes unable to perform immediately prior to or during the fair, it is doubtful if the state will receive sufficient notice to develop alternative means to continue the food and beverage operation without disruption.
- Although rent is not being paid and inadequate insurance is provided, action by the state to terminate the contract is subject to the federal court's approval.

Legislation to enable the following is suggested:

- An authorization for a loan from the General Fund to the Executive Committee to be used only if it becomes necessary for the state to assume control of the food and beverage operations to assure its normal operations.

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- An authorization for an offer to the federal court referee to terminate the existing contract with the following conditions: (1) an immediate payment by the state of the audited unamortized value of the leasehold improvements, less amounts due to the state, (2) the retention of \$200,000 to be paid together with normal profits at the end of the calendar year, and (3) an exclusive food and beverage management contract for 1974 requiring no capital investment.

With my warm best wishes,

Sincerely,



VINCENT THOMAS, Chairman
Joint Legislative Audit Committee

CAL-EXPO
EXCLUSIVE FOOD AND BEVERAGE CONCESSION
CONTRACT TERMINATION

The twenty-year contract with Ancorp National Services, Inc. may be terminated by the following:

- Termination For Cause - The contract specifies the various circumstances under which the state may terminate either directly or upon a failing by the contractor to make correction after being notified of a deficiency. Upon such termination, the contractor is to be reimbursed for the unamortized cost of the leasehold improvements, which is approximately \$2 million at present.
- Termination Without Cause - A court determination of damages for a breach by the state could include not only reimbursements for the unamortized cost of leasehold improvements, but for lost profits as well.
- Mutual Agreement - The contract may be terminated at any time by mutual agreement. However, because the corporation is operating under Chapter 11 of the federal Bankruptcy Act, the approval of federal court referee would be necessary.

TERMINATION FOR CAUSE

Section 10 of the contract requires the following minimum amounts of public liability and property damage insurance: \$1 million for personal injury or death of one person, \$5 million for personal injury or death of two or more persons for each occurrence or event, and \$250,000 for damage to property resulting from each occurrence or event. The original coverage was in these amounts, but the current coverage for two or more persons is \$1.5 million rather than \$5 million.

We informed the Cal-Expo administration of this deficiency. On May 10, 1973, a letter was written to the contractor advising that the insurance coverage should be brought into conformance with the contract. Paragraph C of Section 10 of the contract provides that if the insurance coverage specified is not maintained, the agreement may be terminated.

Section 11 of the contract designates the computation of the monthly payment of rent. A partial payment of the October 1972 rent was made, but no amount has been received for subsequent months. In addition to the unpaid rent on the master food and beverage contract, approximately \$27,500 is owed for utilities, warehouse rent and miscellaneous. The oldest item is from June 1970.

The purpose of the arrangement provisions of the federal Bankruptcy Act is to provide time for the debtor operating under a court-approved plan to work out its financial problems. According to information available to us, some Ancorp operations are being eliminated, but the Cal-Expo operations are to be continued.

Ancorp retains one-half of the rental charges as an offset against the leasehold improvement costs until fully recovered. While the failures to provide the specified amount of insurance and to pay rent are in conflict with the contract, the practical effect is an acceleration of the rate at which rental retention occurs. The unamortized cost of the Ancorp leasehold improvements at Cal-Expo is many times greater than the unpaid rent and the cost of increasing the insurance to the amount specified in the contract.

Termination of the contract which would jeopardize the corporation's ability to resolve its difficulties could subject the state to damages.

MUTUAL AGREEMENT

Any agreement to terminate the lease would have to be approved by the federal referee because the contractor is operating under Chapter XI of the federal Bankruptcy Act. Although Ancorp is operating at present under the arrangement provisions of the act, it could go under the bankruptcy provisions at any time.

If the lease is terminated, the unamortized cost of the leasehold improvements, which according to Cal-Expo records have a current value of approximately \$2 million, is to be paid to the contractor. However, if the contractor becomes bankrupt and thereby unable to perform, the state would probably be allowed to offset against this amount any additional costs or loss incurred as a result of the nonperformance.

The seriousness of the contractor's current financial problems are evidenced by the following:

- For every dollar of current assets there are almost two dollars of current liabilities.
- The total assets are stated to be \$49.5 million, liabilities are \$44.4 million and the stockholders' equity \$5.1 million, which is only a 10 percent equity in the assets.
- The major assets are equipment and leasehold improvements which on an on-going basis may have an actual value equal to or greater than the recorded unamortized cost of \$19 million. However, in the process of liquidating the unprofitable operations, which appears to be a part of the arrangement submitted to the federal court, the amounts actually realized may be considerably less than the stated value.
- The corporate tax liability including withholding from employees and collections from customers is \$3.5 million which is almost six times the cash balance. The nonpayment of taxes could result in the corporation being forced by suppliers to operate on the cash basis which could restrict its ability to meet its contractual responsibilities. The corporation's Cal-Expo operation is seasonal with almost three-fourths of its 1973 annual sales occurring during the four-month period, June through October, and over 55 percent of the annual sales occurring during the 20-day fair period. It is doubtful if the state will receive adequate notice in order to take corrective actions if

the corporation is forced to restrict operations because of its financial condition.

As indicated in our prior report on the Cal-Expo long-term leases, the comparison of food and beverage concession operations with other fairs indicates that the state revenues could be increased substantially by terminating the Ancorp contract. However, at the present time, it does not appear in the state's best interest to pay any more than the recorded amount of approximately \$2 million unamortized costs of the improvement as a consideration for termination. Any additional amount paid could be regarded as a waste of state funds, if shortly thereafter Ancorp becomes bankrupt.

We suggest consideration of the following emergency legislation to insure that food and beverage operations are provided during the 1973 fair and, to enable an immediate offer to be made to the federal referee for the termination of the existing contract and replacement with a one-year food and beverage management contract.

- Authorize a loan to the Executive Committee to be used for food and beverage operations only if Ancorp is unable to perform.
- Provide an appropriation for the audited unamortized value of of the leasehold improvements, less amounts due to the state, with instruction to offer a plan to the federal referee with the following provisions: (1) a termination of the existing lease and a payment by the state for the unamortized value of the leasehold improvements, (2) all of this amount to be paid to

Ancorp upon signing of a new agreement except \$200,000 which is to be deposited in the local bank account to insure operation through the balance of the calendar year, (3) an extension of the existing contract provisions regarding rental to be continued through the balance of the calendar year at which time the local fund is to be transferred to Ancorp and (4) a new contract for 1974 only, designating Ancorp as the food and beverage concession manager for the state with 1) the right to bid on any of the individual concessions and 2) payment for management fee to be negotiated.

This legislation would accomplish the following objectives:

- Assures the food and beverage operations by (1) authorizing a loan in the event Ancorp is unable to perform and (2) retaining a portion of funds offered to terminate the present contract.
- Provides an immediate cash payment to Ancorp upon acceptance of the offer of an amount equal to almost 10 percent of the corporation's total leasehold improvements, which if liquidated in bankruptcy would probably be substantially less and could take years before being settled.
- Permits Ancorp to realize its normal profits through the calendar year, even though most of its investment would be returned upon acceptance of the offer. In addition, Ancorp

would be paid for management service during 1974 and be permitted to bid on individual concessions.

A handwritten signature in cursive script, appearing to read "Walter J. Quinn".

Walter J. Quinn
Acting Deputy Auditor General

May 30, 1973

Staff:
Wesley E. Voss